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BEFORE THE ARIZONA CORPORATION COMMISSION

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AZ CORP COMMISSION
DOCKET CONTROLCOMMISSIONERS

GARY PIERCE, Chairman
BOB STUMP
SANDRA D. KENNEDY
PAUL NEWMAN
BRENDA BURNS

IN THE MATTER OF THE APPLICATION OF
ARIZONA-AMERICAN WATER COMPANY,
AN ARIZONA CORPORATION, FOR A
DETERMINATION OF THE CURRENT FAIR
VALUE OF ITS UTILITY PLANT AND
PROPERTY AND FOR INCREASES IN ITS
RATES AND CHARGES BASED THEREON FOR
UTILITY SERVICE BY ITS ANTHEM WATER
DISTRICT AND ITS SUN CITY WATER
DISTRICT.

DOCKET NO. W-01303A-09-0343

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ARIZONA-AMERICAN WATER COMPANY,
AN ARIZONA CORPORATION, FOR A
DETERMINATION OF THE CURRENT FAIR
VALUE OF ITS UTILITY PLANT AND
PROPERTY AND FOR INCREASES IN ITS
RATES AND CHARGES BASED THEREON FOR
UTILITY SERVICE BY ITS ANTHEM/AGUA
FRIA WASTEWATER DISTRICT, ITS SUN CITY
WASTEWATER DISTRICT AND ITS SUN CITY
WEST WASTEWATER DISTRICT.

DOCKET NO. SW-01303A-09-0343

SUMMARIES OF DIRECT AND SURREBUTTAL TESTIMONY
OF DAN L. NEIDLINGER

Arizona Corporation Commission
DOCKETED

NOV 10 2011

DOCKETED BY

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EXECUTIVE SUMMARY – DIRECT TESTIMONY

Dan L. Neidlinger testifies that:

The Anthem Community Council (“Anthem”) represents over 8,800 of its residents that are water and wastewater customers of Arizona-American Water Company (“AAWC” or the “Company”).

My testimony addresses issues related to the deconsolidation of the Anthem and Agua Fria wastewater operations that are the subject of the Company’s April 1, 2011 Compliance Application ordered by the Arizona Corporation Commission (the “Commission”) in its Decision No. 72047 dated January 6, 2011 (the “Order”) pursuant to a settlement agreement among the Company, Commission staff (“Staff”), the Residential Utility Consumers Office (“RUCO”) and Anthem in an earlier stage of this proceeding.

The underlying need for deconsolidation of the Anthem and Agua Fria wastewater districts is the large difference in cost of service between the Anthem wastewater operations and the Agua Fria wastewater operations. Cost of service is the single most important criterion in the development of fair and reasonable revenues and related rates for a utility in a regulated environment. In this instance, the current rates are not cost-based. Anthem’s wastewater infrastructure is self-contained and is not connected to any of the treatment facilities owned by the Company to serve Agua Fria customers. Further, under present rates, Anthem wastewater customers bear the burden of a significant portion of the costs of Company’s Northwest Treatment Plant (the “Northwest Plant”) which they do not and cannot use. On a consolidated basis, Anthem shoulders a large portion of the estimated \$1.9 million revenue requirement of the Northwest Plant. On a deconsolidated basis, Agua Fria is responsible for 100% of the allocated revenue requirement associated with the Northwest Plant which heretofore has been allocated on a consolidated basis to Anthem and Agua Fria.

On a deconsolidated basis, over \$2.4 million of revenue responsibility is transferred from Anthem to Agua Fria based on the Company’s Statements and Schedules. This is a sizeable shift since it represents 18% of the combined revenue requirement of \$13.3 million authorized in the Order. One of the major reasons for this large disparity is the change, on a deconsolidated basis, in

1 the ratemaking treatment of the Northwest Plant. To address the issue of potential rate shock to
2 Agua Fria customers accompanying the deconsolidation of these two wastewater districts I propose
3 a three-step, three (3) year phase in of the resulting revenue adjustments. Under this plan, annual
4 adjustments of approximately \$800,000 would be made to progressively increase Agua Fria's rates
5 and reduce Anthem's rates. Adjustments would be made to currently approved revenue levels
6 rather than the test year revenue levels shown in the Company's deconsolidation filing. For
7 Anthem, class revenues would be reduced by 9.12% in Step 1, 10.03% in Step 2 and 11.15% in
8 Step 3. Agua Fria class revenues would be increased by 20.95% in Step 1, 17.32% in Step 2 and
9 14.77% in Step 3. Equal percentage adjustments would be applied to each customer class. No
10 upward or downward adjustment is proposed for effluent revenues. The Company would remain
11 whole since there would be no change in overall revenue levels.

12 My testimony also addresses the Company's proposed revenue increases to Anthem's
13 residential and commercial customers in order to recover a short-fall in wholesale revenues from
14 the City of Phoenix (the "City") due to a change of billing practices in 2011 pursuant to the
15 wastewater treatment contract between the Company and the City. This change is clearly outside
16 the scope of the 2008 test year and should not be considered in this limited deconsolidation matter.
17 The recent changes to the wholesale treatment rate charged the City should be dealt with in the
18 next rate case along with the many other changes that have taken place since 2008.

19 As a final matter, I agree with Company witness Sandra L. Murrey in her direct testimony
20 requests that the Commission reconsider "whether a winter-average rate design is appropriate for
21 both districts in the event of rate deconsolidation." The current rate design is preferable to the
22 winter-average rate for a majority of Anthem customers. Moreover, the current design has much
23 better cost of service underpinnings. The postponement of the effective June 2012 date for the
24 winter-average rate design would not, in my view, violate the core findings and mandates of the
25 Order.
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EXECUTIVE SUMMARY – SURREBUTTAL TESTIMONY

Dan L. Neidlinger testifies that:

My surrebuttal testimony is primarily given in response to certain common objections to deconsolidation raised by DMB White Tank LLC (“White Tank”), the Verrado Community Association (“Verrado”), Russell Ranch Homeowners’ Association (“Russell Ranch”) and Corte Bella Country Club Association (“Corte Bella” and, collectively with White Tank, Verrado, and Russell Ranch, the “Intervenors”). The first argument put forth by the Intervenors is that the proposed deconsolidation of the Anthem/Agua Fria wastewater district is premature since the Commission will again address Company-wide consolidation in a future rate case. Second, they assert that Anthem’s support for deconsolidation is inconsistent with my testimony in support of consolidation in an earlier phase of this proceeding. Finally, the Intervenors oppose deconsolidation since it would result in rate shock to the Company’s Agua Fria wastewater customers.

Company-wide consolidation of all of the Company’s water and wastewater districts is not, in my view, imminent. First, the Commission has already rejected consolidation in an earlier phase of this proceeding, based, in part, on wide variances in cost of service among the Company’s districts for both water and wastewater service. These cost of service variances remain today. Further, though the Company has been ordered to present a Company-wide consolidation proposal in a future (but not necessarily the next) rate case, that rate case may be years away and there is no guarantee that the Commission will approve consolidation at that time. Mr. Kent Simer, witness for Verrado, cites in his direct testimony the partial consolidation of Arizona Water Company’s water systems as an indication of the Commission’s intentions with respect to consolidation. In that case, partial consolidation was approved for water systems in close proximity that were interconnected or systems with common water supply. The Anthem and Agua Fria service areas are not interconnected nor are they geographically close. Additionally, the Company already maintains the Anthem wastewater and Agua Fria wastewater districts as “separate business units.” These facts strongly support deconsolidation in the instant proceeding.

1 The benefits of Company-wide consolidation listed in my prior testimony remain valid.
2 However, I am not in favor of Company-wide consolidation unless significant reductions in
3 operating costs could be achieved as a result of consolidation. The Company has indicated that
4 this is not the case, and as a consequence, a critical predicate to my recommendation of
5 consolidation is absent. I also testified that because I was not in favor of any partial consolidation
6 model, should the Commission reject Company-wide consolidation it should also order the
7 deconsolidation of the Anthem/Agua Fria wastewater district.

8 In order to address the Intervenor's concerns about rate shock, my direct testimony
9 proposed a three-step revenue transition plan. Accordingly, rate shock should not be used as a
10 reason for not approving deconsolidation at this time where deconsolidation is necessary to relieve
11 the burden on Anthem wastewater customers created by their subsidization of Agua Fria
12 wastewater customers. My surrebuttal testimony notes that RUCO supports deconsolidation and
13 my proposed revenue transition plan.

14 The Company and Staff neither support nor object to deconsolidation of the Anthem and
15 Agua Fria wastewater districts. In fact, Staff has never taken a position on the issue and Staff has
16 never undertaken any sort of analysis to determine whether the Anthem and Agua Fria wastewater
17 districts should be consolidated for ratemaking purposes.

18 My surrebuttal testimony continues to conclude that ratemaking changes to the wholesale
19 contract with the City of Phoenix are outside the scope of the current case.

20 I also continue to support Ms. Murrey's recommendation that the winter-average rate
21 design be postponed at least until the next rate case.
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